

STATE INVESTMENT COMMISSION
MINUTES
June 25, 2001

The State Investment Commission meeting was called to order by Jonathan Miller, State Treasurer on June 25, 2001 at 3:00 p.m. in Room 264 of the Capitol Annex. Other members present were Orson Oliver, Bank of Louisville; T. Kevin Flanery, Secretary, Finance and Administration Cabinet; and Mike Alexander, proxy for Paul E. Patton, Governor, Commonwealth of Kentucky.

Treasurer Miller confirmed that a quorum was present and that the press had been notified of the meeting. Mr. Flanery made a motion to approve the minutes of the March 21, 2001 meeting of the Commission.

Gordon L. Mullis, Executive Director, Office of Financial Management ("OFM"), provided a brief economic update. Mr. Mullis directed the Commission to Attachment B, *Kentucky Economic Indicators*, a publication of the Governor's Office of Economic Analysis. Kentucky's economy has slowed down significantly. General Fund and Road Fund estimates have been reduced for fiscal year 01 and there will be significant budget reductions in FY02. Manufacturing has slowed significantly in Kentucky causing an impact on sales and use tax, employment growth, and individual income tax. Unemployment remains low in Kentucky. The slowing of the national economy is beginning to impact state revenues. Forty-two of the fifty states are taking measure to reduce expenditures and have revised their official estimates.

Secretary Flanery commented that the Consensus Forecast Group met on June 14 and revised the revenue forecast for FY02 downward by \$321 million.

Mr. Mullis informed the Commission that Mr. Oliver would be presenting an update on the Federal Reserve.

Mr. Oliver stated that it was anticipated that the economic situation would improve by the fourth quarter of this fiscal year. However, officials at the Federal Reserve in St. Louis predict the turn around will not occur until the first or second quarter of FY02. Mr. Oliver provided information concerning how press releases are composed after a Federal Open Market Committee meeting. With this information, not only can the changes in rates that are approved be determined, but also the Committee's concerns about inflation and their bias toward the economy. One additional note contained in the last paragraph in the releases shows the number of Federal Reserve districts that have requested certain actions and is an indicator of the degree to which the twelve members agree.

Mr. Mullis, introduced Resolution SIC 01-02:

**A RESOLUTION OF THE STATE INVESTMENT COMMISSION OF
THE COMMONWEALTH OF KENTUCKY APPROVING
BROKER/DEALER LIST FOR FISCAL YEAR 2002.**

Mr. Mullis indicated that Barclays Capital and SG Cowen Securities Corporation were added as primary dealers at the request of the Commonwealth's securities lending partner. Robert W. Baird & Company and Legg Mason have met statutory and regulatory requirements and have been added as non-primary dealers.

Chairman Miller stated that the Commission previously approved the list and asked why it was being approved again. Mr. Mullis indicated that the Resolution 01-02 was primarily to add the primary dealers. Mr. Mullis also stated that additions or deletions to the broker-dealer list can be made at any time.

A motion was made by Mr. Alexander and seconded by Mr. Oliver to adopt Resolution 01-02 approving the broker/dealer list for FT 2002.

Mr. Price, portfolio manager, Office of Financial Management, presented a portfolio update. Mr. Price provided summary sheets for the individual pools to the Commission members for their review. Mr. Price commented that the modified duration of the bond proceeds pool and the long-term pool fell short of the duration target while the intermediate pool exceeded the duration target. Mr. Price informed the Commission that a wire in the amount of \$576 million for the ALCo TRAN is scheduled for Wednesday, June 27 which has caused the portfolio to be short. However, the cash position should recover on July 3 when \$650 million will be received.

Chairman Miller stated that a recent press report had indicated that part of the revenue short fall was because the portfolio was not earning as much as in previous years. Mr. Price indicated this is a result of a 2.5 percent cutback by the Federal Reserve Board. However, Mr. Price stated that there is more money being managed now than in the past. All budgetary expectations set by the Office of Financial Management have been met. He stated that on a total return basis the portfolio is earning more.

Mr. Mullis added that part of the issue is who owns the securities. He continued that the General Fund does not have a significant amount of cash for the majority of the year and doesn't participate in the earning capacity of the total volume.

Secretary Flanery added that the Commonwealth will borrow \$650 million against the revenue/expenditure mismatch by using revenue anticipation notes. In August, the General Fund will go negative and remain negative through most of the fiscal year because funds are being appropriated and allotted to the agencies. The General Fund recoups its balances in June with receipt of corporate income taxes, sales and use taxes and individual income taxes. Secretary Flanery indicated that declines in sales and use tax and income tax are the major reasons for the revenue shortfall in the Commonwealth.

With no further questions, or business before the Commission, the meeting was adjourned at 3:40 p.m.

Gordon L. Mullis, Secretary
State Investment Commission